

## SUBCOMMITTEE NO. 4

## Agenda

Senator Mike Machado, Chair  
Senator Robert Dutton  
Senator Christine Kehoe



Thursday, April 19, 2007  
10:00 a.m. or Upon Adjournment of Session  
Room 112

Consultant: Bryan Ehlers

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Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

## Departments with Issues Proposed for Vote-only

### 0950 State Treasurer's Office

The State Treasurer, a constitutionally established office, provides banking services for State government with the goals of minimizing interest and service costs, and maximizing yield on investments. The Treasurer is responsible for the custody of all monies and securities belonging to or held in trust by the State; investment of temporarily idle State monies; administration of the sale of State bonds, their redemption and interest payments; and payment of warrants drawn by the State Controller and other State agencies.

The Governor's budget funds 226.6 positions (with 4.0 new positions) and expenditures of \$24.4 million (\$6.6 General Fund).

The Treasurer's Office also plays a central administrative role to the following state boards, authorities and commissions:

<u>Budget Item</u>	<u>Title</u>
0954	Scholarshare Investment Board
0956	California Debt and Investment Advisory Commission
0959	California Debt Limit Allocation Committee
0965	Calif. Industrial Development Financing Advisory Comm.
0968	California Tax Credit Allocation Committee
0971	Calif. Alt. Energy & Advanced Trans. Financing Authority
0977	California Health Facilities Financing Authority
0985	California School Finance Authority

The Treasurer serves as chair or member of these various agencies that organizationally report to the State Treasurer's Office (STO). Several of these agencies are authorized to issue debt for specific purposes as permitted by law. These agencies also may advise California municipalities on debt issuance and oversee the state's various investment operations.

**1. FISCal Support.** The STO requests 4.0 positions and \$481,000 to support the Department of Finance's FISCal technology project. The FISCal project is a long-term IT project to procure a comprehensive statewide financial management system, incorporating budgeting, accounting, procurement, cash management, and related components.

**Staff Comments:** This request conforms to the primary FISCal proposal in the Department of Finance (DOF) budget which was denied by this Subcommittee.

**Staff Recommendation:** DENY the request (to conform with action on the DOF budget).

**VOTE:**

**2. State Boards, Authorities, and Commissions with No Budget Changes.** No changes are requested to the budgets of the following state boards, authorities, and commissions reporting to the STO (see description above):

- 0954 Scholarshare Investment Board
- 0956 California Debt and Investment Advisory Commission
- 0959 California Debt Limit Allocation Committee
- 0968 California Tax Credit Allocation Committee
- 0971 California Alternative Energy and Advanced Transportation Financing Authority
- 0977 California Health Facilities Financing Authority

**Staff Recommendation:** APPROVE the budgets.

**VOTE:**

## **0965 California Industrial Development Financing Advisory Commission**

The California Industrial Development Financing Advisory Commission (CIDFAC) seeks to create employment opportunities and support local economic development by providing low cost financing through the issuance of Industrial Development Bonds (IDBs) to manufacturers through its partnerships with local governments. The CIDFAC is mandated to provide technical assistance to local government issuing agencies such as: cities, counties, economic development authorities, redevelopment agencies, or joint power authorities. Additionally, the CIDFAC independently reviews IDB applications to ensure compliance with federal and state statutes and approves the sale of IDBs by local authorities.

**1. BCP: Appropriation Reduction.** The CIDFAC requests a baseline reduction of one position and \$150,000 to align expenditures with declining revenues.

**Staff Comments:** The CIDFAC relies on revenues from fees associated with its review of IDB applications and approval of the sale of IDBs by local authorities; however, a persistently weak economy over the last four years has suppressed manufacturing finance activity and caused a significant drop in CIDFAC revenues. Although the CIDFAC anticipates that recent federal legislation may make the CIDFAC more attractive and potentially generate future staffing requests, this proposal is intended to better align expenditures with current revenues.

**Staff Recommendation:** APPROVE as budgeted.

**VOTE:**

## **0985 California School Financing Authority**

The California School Financing Authority (CFSA) oversees the statewide system for the sale of revenue bonds to reconstruct, remodel, or replace existing school buildings,

acquire new school sites and buildings to be made available to public school districts (K-12) and community colleges, and to assist school districts by providing access to financing for working capital and capital improvements. The CSFA consists of the following three members: the State Treasurer who serves as chair, the Superintendent of Public Instruction, and the Director of Finance.

**1. BCP: Charter School Facilities Implementation of Proposition 1D.** The CSFA requests \$300,000 in external services funding to meet its Charter School Facilities Program (Program) obligations, which increased from \$400 million to \$900 million when Proposition 1D (The Kindergarten-University Public Education Facilities Bond Act of 2006) was approved by the voters on November 7, 2006.

**Staff Comments:** Combined, Proposition 47 in November 2002, and Proposition 55 in March 2004, and Proposition 1D provide over \$35.5 billion for building new schools and modernizing old facilities, both traditional public and charter schools. Under these measures, the CSFA was funded \$100 million, \$300 million, and \$500 million, respectively. Under state law, CSFA is charged with making a financially sound determination for all Program applicants, conducting ongoing monitoring and due diligence of the financial soundness of each applicant receiving and apportionment; and carrying out due diligence on guarantors.

The CSFA is currently staffed with three positions (including an Executive Director) to process applications for \$400 million in bond funds provided under Proposition 37 and Proposition 55; however, this staffing level is insufficient to address the workload anticipated (review of applications and ongoing determinations of awardee financial soundness) with the addition of \$500 million in funding. Staff notes, statute allows the CSFA to charge administrative costs against bond proceeds, not to exceed 2.5 percent, and subject to Department of Finance approval.

Staff notes, this request was submitted as part of the Governor's January 10 Budget, but was only an initial estimate of needed resources. Based upon additional analysis, a subsequent request (see Issue #2 below) was submitted in April 2007 for 2.0 additional positions and associated funding.

**Staff Recommendation:** APPROVE as budgeted.

**VOTE:**

**2. Finance Letter: Charter School Facilities Implementation of Proposition 1D.** The CFSA requests 2.0 positions (Associate Governmental Program Analysts) and \$129,000 (in addition to the request above—Issue #1) to meet its Charter School Facilities Program obligations, which increased from \$400 million to \$900 million when Proposition 1D (The Kindergarten-University Public Education Facilities Bond Act of 2006) was approved by the voters on November 7, 2006.

**Staff Comments:** See Issue #1.

**Staff Recommendation:** APPROVE the request.

**VOTE:**

## **8910 Office of Administrative Law**

The Office of Administrative Law (OAL) reviews administrative regulations proposed by over 200 state regulatory agencies, and assists those agencies through a formal training program, as well as through less formal methods, to understand and comply with the Administrative Procedures Act. Through its Reference Attorney service, the OAL also provides legal advice to state agencies and members of the public regarding California rule making law. The Governor's budget funds 20.9 positions (including 2.0 new positions) and \$2.9 million in General Fund expenditures.

**1. BCP: Converted Limited-Term Attorney Positions to Permanent.** The OAL requests conversion of 2.0 two-year limited-term positions.

**Staff Comments:** The OAL budget was previously approved as a vote-only item in this Subcommittee; however, concerns were subsequently raised in Assembly Budget Subcommittee No. 4 regarding the OAL's periodic redirection of these positions away from monitoring of underground regulations to other nondiscretionary functions (including reviews of pending regulation). As a result, that subcommittee adopted the Budget Bill Language below requiring the OAL to report on these practices, thereby providing the Legislature with a better understanding of whether the positions are being used for the purpose for which they were approved.

*Item 8910-001-0001, Provision 1.*

*On or before January 10, 2008, the Office of Administrative Law shall report to the appropriate fiscal committees of the Legislature and the Joint Legislative Budget Committee the following information for the 2006-07 fiscal year: 1) the total number of hours the positions assigned to the enforcement of Government Code 11340.5 were diverted away from underground regulation review to other activities of the Office of Administrative Law; 2) a detailed listing of the activities and rationale for the diversion of the positions assigned to the enforcement of Government Code 11340.5; and 3) a listing of the total number of received petitions for investigation of violations of Government Code 11340.5, including the reasons for accepting or declining these petitions.*

**Staff Recommendation:** APPROVE Budget Bill Language (conform to Assembly action).

**VOTE:**

## **9210 Local Government Financing**

The Local Government Financing budget items provide certain types of general financing and law enforcement grants to local governments. Proposed spending in 2007-08 is \$294.3 million (all General Fund)—essentially the same as in the current year. The large reduction of \$1 billion in the current year, compared with 2005-06 is due

to \$1.2 billion of one-time funding provided 2005-06 to make local governments whole for the Vehicle License Fee "Gap Loan."

Several programs are funded in the Budget, including the following:

- **Juvenile Justice Crime Prevention Act.** *The Governor's budget proposes \$119 million for local juvenile justice grants—the same amount as in the current year.*
- **Citizens' Option for Public Safety (COPS).** *The Governor's budget also proposes to maintain COPS funding at \$119 million—the same as in the current year. The program provides per-capita grants for local police departments, sheriffs, and district attorneys.*
- **Rural and Small County Law Enforcement Grants.** *The Governor's budget fully funds this program at \$18.5 million, which provides grants of \$500,000 to 37 counties.*

In addition, the Governor's Budget includes funding for the two programs discussed in the following issues.

**1. Local Detention Facility Fees.** The Administration includes an appropriation of \$35 million for activities associated with local detention facilities. Chapter 1805, Statutes of 2006 (AB 1805, Committee on Budget) established that counties, cities and counties, and certain cities may apply to the Controller to receive funding for local detention facilities and related equipment when an appropriation is made for that purpose. These subventions will be allocated to each county and to cities that operate jails in proportion to each entity's booking fee revenue in 2006-07. Starting in 2007-08, local governments may no longer charge general booking fees. Instead, counties and cities that operate Type One jails may charge a "jail access fee" up to the full cost of processing a booking, but the new fee would be assessed only on the number of non-felony bookings for any local entity that exceed that entity's most recent three-year average of bookings. Arrests for driving under the influence offenses, domestic violence, and violation of protective orders would be excluded from this calculation. If the state provides less than \$35 million in jail subventions in any year, counties and cities could then reinstate general booking fees.

**Staff Comments:** Provision 1 of Item 9210-105-0001 cites Government Code Section 29550, which provides for Booking Fee Subventions; however, the Department of Finance indicates that this is an error—the provision should reference the new jail facility subventions. The citation in the language should be corrected to Section 29552.

**Staff Recommendation:** APPROVE as budgeted with technical correction to cite Government Code 29552 in the Budget Bill Language.

**VOTE:**

**2. Reduction to Redevelopment Bond Debt Backfill.** The Administration proposes to reduce subventions to redevelopment agencies for bond debts by \$1.9 million. This

backfill was created to enable payment of debt service after statute reduced personal property tax subventions to redevelopment agencies. Budget bill provisional language is proposed to reform the allocation of this subvention in accordance with the reduced appropriation.

**Staff Comments:** Provision 3 of the language proposed in the Governor's Budget requires the State Controller to prorate the subventions if they are inadequate to meet debt-service needs. Although the \$800,000 provided in the appropriation should be adequate, it would be preferable to delete the proration language and instead ensure that the full amount needed to pay debt service (beyond the amount of revenues otherwise available to agencies) will be available by adding the following Budget Bill language (as Provision 3):

*Notwithstanding any other provision of law, the Director of Finance may authorize an expenditure in excess of the amount appropriated in this item, to the extent necessary to fund all allocations required pursuant to Provision 2, not sooner than 30 days after notification in writing of the necessity thereof is provided to the chairpersons of the fiscal committees of each house of the Legislature and the Chairperson of the Joint Legislative Budget Committee, or not sooner than whatever lesser time the chairperson of the joint committee, or his or her designee, may in each instance determine.*

**Staff Recommendation:** Approve the item, but replace the proration language in Provision 3 with the Budget Bill Language proposed above.

**VOTE:**

## **9625 Interest Payment to the Federal Government**

These budget items, in accordance with federal law, provide for interest payments on federal funds held by the state in advance of their expenditure. The federal assistance programs affected are those programs that have \$216 million or more in federal fund expenditures. For the majority of these programs, state agencies request federal funds in advance of the warrant (i.e., check) issuance. State agencies use this funding technique because the State Constitution requires that the funds be deposited before the warrants are issued. Interest payments to the federal government are due no later than March 31 each year. The March 31, 2007 payment will be for the interest liability incurred during the state's 2005-06 fiscal year.

The Governor's Budget includes \$30 million from the General Fund and \$900,000 from the State Highway Account in the State Transportation Fund to make estimated interest payments in 2007-08.

**Staff Recommendation:** APPROVE as budgeted.

**VOTE:**

## 9840/9850 Augmentation for Contingencies or Emergencies

These budget items were first adopted in the Budget Act of 2004 to provide a “pay as you go” alternative to the prior practice under which the administration was authorized to “spend at a rate that would result in a deficiency.” Under the new process, the Administration must provide the Legislature with notification of any departmental requests to fund *unanticipated* expenses prior to them being incurred. Approved unanticipated expenses are funded with either a transfer of funds from Item 9840 or a supplemental appropriation sought through legislation.

The Administration’s use of the funds appropriated in Items 9840 and 9850 (\$49 million General Fund, \$15 million each for special funds and nongovernmental cost funds, and \$2.5 million of loan authority) is governed by the provisions of the item, which prohibit the use of these funds for the following purposes: (1) any prior-year expenditure, (2) startup costs not yet authorized by the Legislature, (3) costs that the administration had knowledge of in time to include in the May Revision, and (4) costs that the administration has the discretion to incur or not to incur.

The Administration also may request, via the Chair of the Joint Legislative Budget Committee and the fiscal chairs in each house, enactment of supplemental appropriations bills to augment the amount in this item for specific needs, or if funding needs exceed the amount appropriated in this item. These requests must comply with the similar restrictions to the transfers discussed above.

**Staff Comments:** For the current year, the Governor’s Budget estimates that \$70.5 million (\$45.7 million General Fund) will be spent from this item, and an additional \$703 million (General fund) will be provided in supplemental appropriations bills. The Department of Finance indicates that this amount now has increased by \$28.1 million. The largest amounts of supplemental appropriations have been for the Department of Mental Health (past liabilities for Early and Periodic Screening, Detection, and Treatment—EPSDT—services) and for the Department of Corrections. The budget does not include any set-aside for supplemental appropriations in 2007-08 although they generally total hundreds of millions of dollars annually.

**Staff Recommendation:** APPROVE as budgeted.

**VOTE:**



## Departments with Issues Proposed for Discussion

### 0860 Board of Equalization

The State Board of Equalization (BOE), the Franchise Tax Board (FTB), and the Employment Development Department (EDD) are the state's major tax collection agencies. The BOE collects state and local sales and use taxes and a variety of business and excise taxes and fees, including those levied on gasoline and diesel fuel, alcoholic beverages and cigarettes, as well as others. BOE also assesses utility property for local property tax purposes, oversees the administration of local property tax by county assessors, and serves as the appellate body to hear specified tax appeals, including FTB decisions under the personal income tax and bank and corporation tax laws.

The Governor's budget funds 3,800.5 positions (including 80.9 new positions) and proposes \$390.2 million in total expenditures (\$218.1 million General Fund).

#### ***DISCUSSION ISSUES:***

**1. Informational Issue: Recruitment and Retention.** In recent years, the BOE has experienced problems in recruitment and retention, resulting in high vacancy rates, particularly among auditors, that threaten state revenues.

**Staff Comments:** At the previous hearing, the BOE reported to the Subcommittee on recent efforts it has made to address the recruitment and retention issue, and indicated progress has been made toward reversing the trends noted above. The Chair requested the BOE to provide the Subcommittee with an assessment of potential barriers to continued vacancy reductions and plans to address those barriers. The BOE response (see below) identified: (1) salaries and (2) the exam process as the two main areas of concern, and highlighted the need to work with the Department of Personnel Administration and the State Personnel Board to address these challenges.

#### **1. Salaries**

- **Competitiveness:** Potential candidates and some experienced BOE employees leave the agency for "higher-paying" jobs in county, federal or private domains.
- **Compaction Issues:** Both BOE and service-wide classes are affected by the salary inequities that currently exist. In some cases, employee's salaries are higher than those of the supervisor.

#### **BOE Proposed Solution**

*BOE will continue to work with the Department of Personnel Administration (DPA) in identifying salary issues as they relate to specific BOE classifications. BOE will work with the DPA to address compaction issues. In addition, the BOE will continue to pursue permanent hiring above minimum provisions for auditor and compliance series.*

## **2. Exam Process**

- Complexities exist with the current exam process.

### **BOE Proposed Solution**

*BOE will work with the Department of Personnel Administration and the State Personnel Board to establish deeper classes in order to streamline examination process and eliminate multiple exams to progress through a promotional series.*

**2. BCP: E-Filing Infrastructure Project.** The Governor's Budget proposes to expand BOE's SUT electronic filing program to include businesses with multiple locations and those required to pay with electronic funds transfer (EFT), and to automate the delinquent prepayment process and make other improvements. To accomplish these goals, the administration requests two positions and \$1,460,000 (\$949,000 General Fund and \$511,000 reimbursements) in 2007-08, and three positions and \$431,000 (\$280,000 General Fund and \$151,000 reimbursements) in 2008-09.

**Staff Comments:** The BOE has been converting to electronic technologies in the filing and processing of tax returns and remittances, which has advantages to both taxpayers (minimizing record keeping requirements, increased filing accuracy, and reduced costs) and to tax agencies (decreased processing time, reduced storage costs, fewer staff needed, improved data accuracy, and easier information exchange for enforcement and compliance purposes). Additionally, processing electronically filed returns and remittances costs a fraction of the costs associated with paper documentation.

At a previous hearing, the Subcommittee heard concerns raised by the LAO that, although this proposal represents stage three of a plan to move the agency and the taxpayers it serves towards a more electronically integrated business model, estimates of savings to the state had yet to be quantified. Consequently, the Chair requested the BOE to report back with its best estimate of possible out-year savings in order to provide the Subcommittee with some sense of the potential magnitude.

The BOE has since provided legislative staff with the following table of potential savings estimates:

<b>Fiscal Year</b>	<b>Participation Level</b>	<b>Potential Personnel Year Savings</b>	<b>Potential Direct OE&amp;E Savings<sup>1</sup></b>	<b>Potential Total Savings<sup>2</sup></b>
2008-09	10%	\$794,897	\$132,565	\$927,462
2009-10	20%	1,589,794	265,130	1,854,924

Staff notes that the BOE is still unwilling to speculate on potential savings in 2007-08 because the program is still in its early stages and data is unreliable; however, the BOE indicates that beginning in 2008 e-filers will have the option of remitting payment by

<sup>1</sup> Operating expense and equipment (OE&E) includes general expense, printing, postage, communications, insurance, and other miscellaneous.

<sup>2</sup> Excludes facilities costs that are fixed and would only result in cost avoidance savings should the BOE need to obtain lease space outside the headquarters facility.

check (currently they must use e-payment), and this is anticipated to have a marked impact on participation levels. For example, the e-filing participation rate is currently 2.5 percent, but the BOE expects it to quadruple by 2008-09 as the result of the new remittance policy combined with the following filing strategies the department intends to pursue to market e-filing:

- ***Combine Seller's Permit and E-Client Registration Process***  
Individuals selling tangible personal property in California must register for a seller's permit with the BOE. At the time of registration for a seller's permit, the BOE plans to also register taxpayers for e-filing.
- ***Discontinue Sending Paper Tax Returns***  
Paper tax returns are sent to sales and use taxpayers that report either on a monthly, quarterly, fiscal yearly or calendar yearly basis whether or not they e-file (unless the taxpayer has elected to no longer receive paper returns). The BOE is developing a pilot project to discontinue sending paper returns to certain taxpayer groups.
- ***Outreach Efforts***  
The BOE has developed an Outreach Plan that will focus on new and innovative approaches to marketing e-services, such as on-line tutorials/videos, focus groups and speaking engagements.

While e-filing promises to be the technology of the future in collecting state revenues, the data above indicates that far higher levels of participation are necessary before the state will see significant savings. In the short term, the Subcommittee may wish to consider Budget Bill Language to require the BOE to keep the Legislature informed of steps taken and progress achieved toward the 10 percent participation projected for 2008-09. Additionally, the Legislature may wish to consider future legislation to mandate e-filing (as has been done in various other states) to ensure participation and capture the full potential savings of this technology.

**Staff Recommendation:** APPROVE the request with Budget Bill Language requiring the BOE to report to the Legislature no later than March 1, 2008, on steps taken and progress achieved toward reaching a 10 percent participation level in its e-filing program.

## **VOTE:**

### ***VOTE-ONLY ISSUES:***

**1. BCP: Continuation Of International Fuel Tax Agreement (IFTA)/North American Free Trade Agreement (NAFTA) Interim Program.** The Administration requests authority to spend \$842,000 (federal funds) in the budget year and establish 8.5 limited-term positions during the same period. This funding will support program enhancements necessary to allow the BOE to continue hosting Mexican Truckers in the IFTA and ensuring that Mexican truckers properly report and pay fuel taxes in California.

**2. BCP: Motor Vehicle Fuel Audit Staff Augmentation.** The Administration requests \$715,000 (Motor Vehicle Fuel Account) and 5 audit positions to take advantage of new data generated by an automated reporting system and ensure tax compliance within the BOE's transportation tax programs; the motor vehicle fuel tax, diesel fuel tax, and jet fuel

tax. The BOE anticipates revenues of \$14 million associated with these positions, a 21:1 benefit-cost ratio, while the DOF projects \$19 million.

**STAFF RECOMMENDATION ON VOTE-ONLY ITEMS:** APPROVE AS BUDGETED.

**VOTE on Vote-Only Issues 1-2:**

## 1730 Franchise Tax Board

The Franchise Tax Board (FTB) administers state personal income tax and corporation taxes for the State of California, collects debt on behalf of other state agencies and local entities, and performs audits of campaign statements and lobbyist reports authorized by the Political Reform Act of 1974. The FTB is tasked to correctly apply the laws enacted by the Legislature; to determine the reasonable meaning of various code provisions in light of the legislative purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view. The Governor's budget funds 5,174.5 positions (including 240.7 new positions) and expenditures of \$623.4 million (\$518 million General Fund).

### ***DISCUSSION ISSUES:***

**1. BCP: Tax Gap.** The FTB estimates that the tax gap, the difference between what taxpayers actually pay and what they should pay, is around \$6.5 billion/year. In a typical tax year approximately 89 percent of all taxes owed are ultimately paid, with the remaining 11 percent constituting the tax gap. The tax gap is harmful to the state in many ways, but principally because: (1) those who pay their fair share pay higher taxes to cover the gap, and (2) tax collections are undermined by the public perception that some are not paying their fair share.

The tax gap is manifested in three forms: manipulated tax filings through underreporting of income and overstating deductions, nonfiling of tax returns, and underpayment of amounts owed. Underreporting income and overstating deductions is by far the most common form (80 percent of total) with nonfiling and underpayments making up the remaining causes (about 10 percent each).

The Administration requests funding of \$19.6 million General Fund and 230 positions to support existing efforts to narrow the tax gap and develop new initiatives to further close that gap. Anticipated revenues in the budget year are approximately \$77.5 million in the budget year. These important and far-reaching proposals include the extension of positions and activities approved in prior budgets. The continuing initiatives include efforts to detect preparers of fraudulent returns, identifying new information sources to identify non-filers, and augmenting audit and collections staff.

The new initiatives focus on longer-term approaches to narrowing the tax gap and are based on a recently developed strategic plan to address the tax gap. They include: expanding the corporate non-filer program, addressing out-of-state tax avoidance, and improving methods for detecting under reporters.

Consistent with past years' practice, the Legislature will seek to clarify the benefits of these initiatives, gauge the impact on taxpayer behavior, and explore other means to narrow the \$6.5 billion tax gap even further.

**Staff Comments:** In its analysis of the Governor's Budget, the LAO noted concerns with this proposal and recommended redirecting some of the proposed funding to tax gap enforcement activities with a higher benefit-to-cost ratio. While the LAO remains a proponent of providing funds where they will generate the most General Fund revenue, based on additional information from the FTB the LAO now recommends the following:

- Reallocate \$865,000 from the proposed Underground Economy Criminal Investigations program, with \$615,000 directed to augment the Corporate Nonfiler program (which has a significantly higher benefit-cost ratio), and reserve \$250,000 to pay a portion of contractor expenses associated with assessment of a “software overlay” approach for the three tax agencies (per LAO’s Report on Tax Agency Information and Data Exchange). [Staff notes this issue was heard previously in this Subcommittee and the agencies continue to work toward developing a proposal to present to the Legislature.]
- Given the low benefit-cost ratio (BCR) of 2.2:1 reported for the Underground Economy Criminal Investigations program, fund the program on a two-year limited-term basis to allow for a future reevaluation.

The LAO estimates the above recommended changes to the proposed tax gap initiatives would generate approximately \$2 million of additional General Fund revenue in the budget year at the same overall level of expenditures contained in the Governor’s Budget.

**Staff Recommendation:** APPROVE the LAO recommendation.

**VOTE:**

**2. Additional Savings from E-Services.** The LAO points out that information provided by FTB indicate ongoing growth in electronic filing of returns and remittances. This growth has occurred as a combined result of statutory mandates for tax practitioners as well as a natural migration from paper to electronic filing by individual and business taxpayers as society becomes increasingly computer oriented. The department reports that it expects 9 percent annual growth in electronic remittances through 2008, and 4 percent to 7 percent annual growth in electronic returns over the same period.

Reflecting the growth in electronic filings and remittances—and the large savings associated with the use of this technology—the department’s budget for processing has been reduced almost every year since 2001-02. These annual reductions ranged from \$400,000 to about \$1 million.

The 2007-08 budget includes savings of \$298,000 due to increased electronic filing for the Personal Income Tax (PIT). However, no budget reductions were proposed related to increased electronic remittance processing or reductions in mailed and printed tax forms and booklets due to more use of online forms and other information. The board is also expanding the Business Entities E-File (BEEF) system, but did not account for any savings associated with increased electronic filing of BEEF returns.

**LAO Recommends \$500,000 Reduction to Capture Savings.** Based on information provided by FTB, LAO recommends a reduction of \$500,000 for 2007-08 to account for savings associated with increased use of business-entity electronic return processing, electronic remittance processing, and associated reductions in the amount of paper printing and mailings.

**Staff Comments:** At a previous hearing, the FTB indicated that it would prefer to retain the savings identified above in order to offset the potential impact of the unallocated reduction that is proposed in the Governor's Budget (\$100 million in Control Section 4.05 plus an additional \$46 million in Control Section 4.04). The Chair requested the FTB and the DOF to work with staff and the LAO to review the potential impact of the unallocated reduction.

In subsequent conversations, the DOF indicated that the FTB could absorb \$900,000 of the unallocated reduction within its Operating Expense and Equipment budget, but would likely need to delay filling new positions if it were required to absorb the remaining \$500,000 proposed in the Governor's Budget. According to the DOF, this would necessitate programmatic reductions that could impact General Fund revenues; however, the DOF did not specify which program areas would be affected.

Staff notes that the \$500,000 savings that is in question was identified by the LAO, and was not factored into the Administration's proposed unallocated reductions. Therefore, the Subcommittee should request an explanation of how the Administration originally expected the FTB to take the reductions without impacting revenues. Additionally, staff notes that the Director of Finance has the discretion to provide departments with target reduction amounts and therefore the DOF could adjust the FTB's share of the unallocated reduction if General Fund revenues were going to be adversely impacted.

**Staff Recommendation:** APPROVE the LAO recommendation and reduce the FTB budget by \$500,000.

**VOTE:**

**3. BCP: Legal Support for Abusive Tax Shelters.** The Administration requests \$1.3 million and 10 new positions to address Abusive Tax Shelter workloads.

**Staff Comments:** In a previous hearing, the Chair requested clarification on the magnitude of the problem of abusive tax shelters and the staffing required to address them (including in out-years).

The FTB response indicates that the extent of the problem of abusive tax shelters is not well documented because users of tax shelters actively seek to avoid detection. However, based on what is known, the FTB believes that there is sufficient workload to merit the staffing requested and that this investment will result in additional revenues of approximately \$1.4 billion (above and beyond the \$1.4 billion collected during the Voluntary Compliance Initiative (VCI), but inclusive of the additional \$348 million in subsequent tax shelter assessments). Given the extreme complexity of abusive tax shelter cases, the combativeness of representatives and investors, and the fact that the VCI accelerated the easiest cases, the FTB has estimated that it may take up to eight years to collect this revenue.

According to the FTB, while the Abusive Tax Shelter program has been a success, there is no indication that abusive tax shelters will go away at any time in the near future. The FTB expects that as California's economy continues to grow and global competition increases, individuals and companies will continue to seek ways to minimize their tax burden, and the products available will constantly seek to push, and ultimately step over,

the line between tax planning and tax abuse. For example, even after nearly a decade of discussion and calls for better enforcement at the federal level, the U.S. Senate Permanent Subcommittee on Investigations reported, in August 2006, a loss of over \$100 billion annually from offshore tax havens and tax shelter abuses. The FTB believes that high profile enforcement and public disclosure will continue to make a big dent in abusive tax shelter investments and discourage investors from considering abusive schemes; however, constant vigilance will be the only mechanism to successfully control the proliferation of new iterations of tax shelter schemes.

The FTB does not project that additional auditor, attorney, or collector position requests will be made in the future to produce the \$1.4 billion in revenue currently estimated to be realized from the abusive tax shelter program. Should the FTB's efforts identify a new inventory of tax shelter cases which will generate additional revenues and require resources, the department would redirect resources from lower cost-benefit workloads and/or present the Legislature with the opportunity to fund those workloads.

The LAO previously articulated concern over the future staffing needs of this program, noting that while attorneys may be necessary to process the up-front workload, collectors and auditors would likely be necessary as well. However, the FTB has clarified that while the targets of the requested attorneys are generally well-funded, they are relatively few in number. Thus, the FTB expects that audits and collections activities could be handled within existing resources. Given this clarification, the LAO and staff have withdrawn their concerns.

**Staff Recommendation:** APPROVE as budgeted.

**VOTE:**

**4. BCP: Restoration to Customer Service Level.** The administration requests \$1.3 million and 27 positions to restore staffing levels in the Franchise Tax Board's Contact Centers and related supporting workloads. These call center positions were eliminated in recent years to meet budget reduction targets and the department now asks that they be restored in order to restore taxpayer and tax practitioner customer service and meet a response target of responding to 95 percent of all calls with 80 percent answered within 2 minutes.

**Staff Comments:** In a previous hearing, the Subcommittee learned that this request would improve the level of calls answered from 73 percent to 83 percent, but would not achieve the FTB customer service goal identified above. The Subcommittee heard discussion as to whether this incremental improvement in service was worth the \$1.3 million cost of this proposal, and the Chair requested the FTB to provide the Subcommittee with monthly estimates of call volumes, answer rates and wait times. Additionally, the Chair asked the FTB to work with staff and the LAO in discussions about an adequate level of service within the framework of the unallocated reduction addressed in Issue #2 (above).

In response to the Chair's request, the FTB provided the tables below which reflect the Level of Access (LOA), Level of Service (LOS) and Average Wait Times associated with current and proposed staffing levels. The LOA represents the percentage of calls the answered by an FTB Customer Service Representative (CSR) compared to total calls



received, while the LOS represents the percentage calls answered within the FTB's two-minute target time period. The Average Wait Time represents the time a caller spends on hold waiting to talk to a live agent after their call has been received by the Interactive Voice Response (IVR) system and they have made a selection to request to speak to a CSR. Staff notes, the amount of time a caller spends "surfing" the IVR is not included in these statistics, nor does the FTB record this data.

As Table 1 indicates, existing staff levels provided an average LOA of approximately 67 percent in 2006, meaning that 33 percent of callers (nearly 700,000) seeking to speak to a CSR failed to do so. Notably, the percentage of calls answered in each month (LOA) does not necessarily correlate directly to the level of calls "offered" (that is, the number of calls received by the IVR system). While the highest LOA corresponds to the lowest level of calls (in December) and the lowest LOA corresponds to the highest level of calls (in May), the LOA remains relatively low (hovering between 50 and 60 percent) throughout the months of June, July, and August, even as calls decline by almost 50 percent from the peak over that period. The Subcommittee will want the FTB to speak to these trends and identify potential solutions to increase the number of calls answered during these months of the year.

**Table 1 – Level of Access (LOA) for 2006**

	<b>Offered</b>	<b>Answered</b>	<b>LOA</b>
06-Jan	121,553	101,330	83.40%
06-Feb	239,529	175,331	73.20%
06-Mar	269,817	201,619	74.70%
06-Apr	265,170	189,476	71.50%
06-May	320,076	130,952	40.90%
06-Jun	222,774	129,564	58.20%
06-Jul	182,435	95,458	52.30%
06-Aug	152,604	84,870	55.60%
06-Sep	97,002	90,620	93.40%
06-Oct	100,364	89,494	89.20%
06-Nov	86,528	74,220	85.80%
06-Dec	80,155	72,718	90.70%
	<b>2,138,007</b>	<b>1,435,652</b>	<b>67.15%</b>

Table 2 (see next page) breaks down the LOA shown in Table 1 into Peak and Non-Peak averages, and additionally shows the LOS and Average Wait Time associated with these periods. The FTB defines the Peak period as January through June, thus, the relatively low LOA of 72.6 percent for the Non-Peak period is due to the fact that the averages for July and August (approximately 52 percent and 56 percent, respectively) skew the average for the remainder of the months (which tend to hover in the vicinity of 90 percent). Table 2 indicates that during the Peak period only 15 percent of callers requiring a human response made contact with a CSR within 2 minutes, and in fact the Average Wait Time was over 6 minutes. During the Non-Peak period, customer service improved to only 40 percent of calls answered by a CSR within 2 minutes and an average wait of approximately 4 minutes.

**Table 2 – Level of Access (LOA), Level of Service (LOS), and Wait Times Over Peak and Non-Peak Periods for 2006.**

Level of Access			Level of Service			Average Wait Time	
Peak	Non-Peak	Total Average	Peak[1]	Non-Peak[1]	Total Average [1]	Peak[2]	Non-Peak[2]
64.5%	72.6%	67.1%	15.2%	40.6%	24.1%	6:17	4:08

[1] This percentage is a weighted average. [2] Although this is the average wait time, some callers waited 30-40 minutes to speak with a agent.

Table 3 uses the same display as Table 1, but reflects FTB projections of the call workload to be addressed by the proposed new staff in Fiscal Year 2007-08. Based on call volumes similar to 2006, the FTB expects this \$1.3 million proposal to enable it to answer approximately 14 percent more calls (or 294,000) over the course of the year. This equates to a cost of \$4.42 per additional call answered; however, it is necessary to view Table 4 to get a sense of what the proposed expenditure would buy in terms of improved LOA and Average Wait Time.

**Table 3 – Projected Level of Access (LOA) for Fiscal Year 2007/08 (Including 27 Positions Requested)**

	Offered	Answered	LOA
06-Jan	121,553	115,475	95.00%
06-Feb	239,529	216,718	90.48%
06-Mar	269,817	244,296	90.54%
06-Apr	265,170	233,434	88.03%
06-May	320,076	167,130	52.22%
06-Jun	222,774	162,423	72.91%
06-Jul	182,435	127,242	69.75%
06-Aug	152,604	116,797	76.54%
06-Sep	97,002	92,152	95.00%
06-Oct	100,364	95,346	95.00%
06-Nov	86,528	82,202	95.00%
06-Dec	80,155	76,147	95.00%
	2,138,007	1,729,362	<b>80.89%</b>

Assumptions: (1) same level of "offered" calls by month as 2006 calendar year; (2) resources are allocated in a manner consistent with current allocation; and (3) methods of workload management are applied.

Table 4 breaks the Fiscal Year 2007-08 projections into Peak and Non-Peak and displays the LOS and Average Wait Time for these periods. As compared to Table 2, the proposal would improve Peak LOS by approximately 25 percent and decrease Average Wait Time during peak months by approximately 1 minute and 45 seconds. During the Non-Peak period, the proposal would increase LOS by approximately 25 percent, but Average Wait Time would remain relatively constant at 4 minutes per call. This last conclusion appears counter-intuitive, but would seem to suggest that despite fewer calls during the Non-Peak period, the length of the average call (perhaps due to

the complexity of questions) increases significantly. The Subcommittee should request the FTB to clarify this issue.

**Table 4 – Projected Level of Access (LOA) and Level of Service (LOS) and Average Wait Time Over Peak & Non-Peak Periods for Fiscal Year 2007/08 (Including 27 Positions Requested)**

PEAK	Offered	Answered	LOA	LOS	Avg. Wait Time
Jan-Jun	1,438,919	1,139,476	79.19%	40%	4:30

NON-PEAK	Offered	Answered	LOA	LOS	Avg. Wait Time
Jul-Dec	699,088	589,886	84.38%	65%	4:00

Overall, this proposal would provide an incremental increase in calls answered (at a cost of approximately \$4.42 per call) and a reduction in wait times during the Peak period of the year. The optimal or desirable level of service to provide to FTB customers is a policy decision that must be weighed against other pressures on the General Fund; however, based on the FTB's own criteria, this proposal would result in progress toward achieving the department's customer service goals. If the Subcommittee decides to approve this proposal, it may wish to require the FTB to report on actual customer service outcomes in order to better inform future deliberations on customer service should those discussions arise.

**Staff Recommendation:** APPROVE as budgeted with Budget Bill Language requiring the FTB to report on actual customer service outcomes resulting from the additional staffing.

**VOTE:**

**VOTE-ONLY ISSUES:**

**1. BCP: E-Commerce Portal Infrastructure.** The Administration requests \$1.5 million General Fund and one position to replace the current Internet infrastructure at the Butterfield Way campus in Sacramento and provide redundancy to accommodate growth in the FTB's e-commerce programs. These programs facilitate taxpaying by providing online filing services and other capabilities previously done by mail or phone. This request represents year one of a three-year project of which total costs are expected to be \$4.5 million.

**2. Centralized Reverse Proxy Services.** The Administration requests to redirect \$298,000 in e-file savings (first realized in the current year) to enhance the security of FTB's Internet servers. Centralized Reverse Proxy Services will provide additional protection against unauthorized access via the Internet by allowing for only one well-guided point of entry and thereby resolving several data security vulnerabilities.

**STAFF RECOMMENDATION ON VOTE-ONLY ITEMS:** APPROVE AS BUDGETED.

**VOTE on Vote-Only Issues 1-2:**

## **1760 Department of General Services**

The Department of General Services (DGS) provides management review and support services to state departments. The DGS is responsible for the planning, acquisition, design, construction, maintenance, and operation of the state's office space and properties. It is also responsible for the procurement of materials, data processing services, communication, transportation, printing, and security. The Governor's budget funds 3,703 positions (including 67.5 new positions) and \$1.2 billion in expenditures, of which \$9.2 million is from the General Fund.

### ***DISCUSSION ISSUES:***

**1. BCP: Fleet Analysis and Reporting System.** The budget includes a request for two positions and \$614,000 in 2007-08 (Service Revolving Fund) and four positions and \$1.3 million (Service Revolving Fund) in 2008-09 to continue development of a Fleet Analysis and Reporting System to improve tracking state vehicles. Once fully implemented, the department expects revenues in excess of \$2 million from surplus vehicle sales.

**Staff Comments:** According to the DGS, as of December 2005, the executive branch owned 51,628 vehicles, including approximately 37,000 passenger vehicles (or nearly 72 percent of the fleet), of which 31,766 were gasoline-powered sedans, SUV's, and light duty trucks, 4,892 were alternative fuel vehicles, and 357 were hybrid vehicles. Although nine agencies own 82 percent of the passenger fleet and 119 agencies own at least one vehicle, only the DGS, the California Highway Patrol, Caltrans, Parks and Recreation, and the Department of Water Resources have a fleet management system in place. Altogether, only 60 percent of the state fleet is covered by an asset management system.

The system under DGS development is a data warehouse that will extract information from existing fleet management systems and provide statewide reporting and analysis capabilities. Given immediate access to current and accurate fleet data, the DGS Office of Fleet Administration will be able to perform analyses to estimate green house gas emissions, identify underutilized vehicles, and produce reports that may be used to right-size the statewide fleet – simultaneously reducing taxpayer costs and carbon footprint.

At the a previous hearing, the Chair requested the DGS to work with the LAO to develop performance measures so that the Subcommittee could adopt Budget Bill Language requiring the DGS to report on project outcomes. The DGS responded with the following program objectives:

OBJECTIVE	MEASURE
1. Improve Vehicle Utilization for the Statewide Fleet	98 percent of Statewide fleet meets current utilization targets within 2 years of system implementation.
2. Dispose of Vehicles not Meeting Minimum Utilization Standards	Dispose of at least 75 percent of vehicles not meeting minimum utilization standards.
3. Lower Total Cost of Ownership for the Statewide Light Duty/ Passenger vehicles	Reduce the Statewide Light Duty/Passenger Fleet size by eliminating 4.6% excess of obsolete vehicles.
4. Improve Fleet Fuel Efficiency	Improve the average miles per gallon (MPG) for the Statewide fleet from the initial baseline for five consecutive years.
5. Reduce Time Required to Prepare Standard / Ad Hoc Statewide Reports	Reduce the time necessary to prepare/respond to statewide reports from an average of 2-4 months to two business days for standard reports and five business days for ad hoc reports.
6. Meet State and Federal Reporting Mandates	DGS will meet 100% of State and Federal Reporting mandates.
7. Create one-time savings through the sale/repurposing of underutilized vehicles	\$2.4 million achieved in one-time net savings.

The objectives and measures proposed by the DGS above generally provide a useful basis for identifying and quantifying progress toward successful implementation of the Fleet Asset Management System. However, staff notes concern that the proposed fuel efficiency measure lacks specificity, and the DGS has not identified the baseline MPG. Since the proposed goal of improving the average MPG for the fleet over five consecutive years could be achieved by posting only meager gains (e.g. 0.01 MPG per year), the Subcommittee will want the DGS to commit to a specific MPG target or a national annual bench mark.

Pursuant to the Chair's request, the DGS also worked with staff and the LAO to develop the following Budget Bill Language requiring the DGS to report on progress toward the above objectives:

*Item 1760-001-0666, Provision X*

*The Department of General Services shall report to the Department of Finance and the appropriate fiscal committees of the Legislature on April 1, 2009 to provide an implementation progress report and on April 1, 2010 to provide the status of the following areas: (1) Progress on meeting statewide fleet utilization targets; (2) Disposal of vehicles not meeting minimum utilization standards; (3)*

*Trend of statewide fleet size; (4) Trend of statewide fleet average fuel efficiency; (5) Timeframes associated with producing standard and ad hoc reports; and (6) Savings and cost avoidances achieved to date and potential for additional savings and cost avoidances.*

**Staff Recommendation:** APPROVE with Budget Bill Language.

**VOTE:**

**2. BCP: Support for the Governor's Executive Orders on Energy Efficiency and Green Buildings.** The Administration requests 5.0 positions and \$428,000 (Service Revolving Fund) to support the Bureau of Property Management's (BPM) implementation of Executive Orders S-12-04 and S-20-04 which require DGS to reduce energy purchases for state-owned buildings and to design, build, and operate "greener" buildings.

**Staff Comments:** This request (as well as the request in Issue #4 below) is part of a \$13.8 million, six-year project to meet the energy conservation and efficiency goals articulated in Executive Orders S-12-04 and S-20-04. According to the DGS, existing staffing levels are insufficient to support the additional workload created by the executive orders.

**Executive Order S-12-04** directs the DGS to institute energy conservation measures that will reduce energy consumption during stage II electrical emergencies in advance of private actions that occur in state II and stage III electrical emergencies. Additionally, state agencies are required to pursue energy consumption reduction measures at all facilities where conservation can be achieved cost effectively.

**Executive Order (EO) S-20-04** commits the state to reducing state-building electricity usage by retrofitting, building and operating the most energy- and resource-efficient buildings by taking all cost-effective measures described in the Green Building Action Plan (GBAP) for state-owned buildings. The EO also directs agencies to undertake measures to reduce grid-based energy purchases for state-owned buildings by 20 percent by 2015. Included in these measures are designing, constructing, and operating all new and renovated state-owned facilities paid for with state funds as "LEED Silver" or higher certified buildings (based on the Leadership in Energy and Environmental Design rating system for existing buildings—LEED-EB).

Staff notes that the goals of the EOs above are substantially in line with the broader aims of Chapter 488, Statutes of 2006 (AB 32, Nunez)—the Global Warming Solutions Act of 2006, which requires the Air Resources Board to adopt regulations to reduce statewide greenhouse gas emissions (GGEs) to 1990 levels by 2020. However, it is not entirely clear how or whether the energy efficiency efforts being pursued in this request fit into a comprehensive state policy to implement AB 32. The Subcommittee will want the DGS to clarify the relationship between this request and the requirements of AB 32, and explain how this request fits into an overall strategy for reducing of GGEs in the most cost-effective manner possible (i.e. at the highest benefit-to-cost ratio).

**Staff Recommendation:** HOLD OPEN.

**3. BCP: Private Consultants for Green Building Initiative.** The Administration seeks \$3.0 million (Service Revolving Fund) to secure private consultants to pursue Leadership in Energy and Environmental Design rating system for existing buildings (LEED-EB) goals for eleven state office buildings. This energy efficiency goal ties to Executive Order (EO) S-20-04. Consultants will conduct in-depth evaluations of building operations and train building managers on how to operate a more energy efficient building. The cost for this consulting service will be shared by the departments occupying the eleven affected buildings.

**Staff Comments:** This request is a counterpart to the proposal in Issue #3 and is reflective of the fact that LEED-EB certification is highly technical and requires engineering expertise specific to the performance factors considered for LEED-EB accreditation.

The Subcommittee will again want the DGS to clarify the relationship between the request and the requirements of AB 32, and explain how these energy efficiency efforts fit into a comprehensive state policy for the maximum reduction of GGEs at the least possible cost. Additionally, given the Administration's long-term goal to reduce energy use in state-owned building by 20 percent by 2015, the Subcommittee may wish to inquire why the DGS plans to use the \$150/hour consultants ongoing instead of training state employees over time to replace the consultants at a more moderate rate of compensation.

**Staff Recommendation:** HOLD OPEN.

**4. BCP: Augmentation for Building Security Services.** The Administration requests \$1.1 million (Service Revolving Fund) to fund increased costs contained in the Master Security Services Agreement for 15 state buildings. This agreement and procurement of private security services is overseen by the California Highway Patrol, who had previously provided security services for these buildings.

**Staff Comments:** This Subcommittee heard a similar issue last year and raised concerns that the state has no standard security requirement for its buildings, and that since 9/11 requests for security augmentations have occurred on a piecemeal basis. Budget Bill Language was subsequently included to require the DGS to report on the nature and level of security expenditures at state-owned buildings of 50,000 square-feet or more. Staff notes that the report was due to the Legislature by March 15, 2007, but has yet to be submitted. Because the Subcommittee will want the DGS to speak to the need for this proposal within the context of the report findings, further discussion on this issue should await a future hearing after the report has been released.

**Staff Recommendation:** HOLD OPEN.



**VOTE-ONLY ISSUES:**

**1. Capital Outlay BCP: Renovation of H and J Buildings—Patton State Hospital.**

The budget includes \$4.0 million (Earthquake Safety Bond Funds) for preliminary plans and working drawing phases of a project to create intermediate “swing space” and seismically renovate four buildings at the hospital. Due to growth in the hospital population at all state hospitals, the Department of Mental Health is unable to relocate the patients during construction.

**2. Capital Outlay BCP: Structural Retrofit—Sierra Conservation Center, Department of Corrections Jamestown Facility.** The Department of General Services requests \$168,000 (Earthquake Safety Bond Funds) for working drawings for the California Department of Corrections Jamestown Buildings E and F. DGS has determined these structures to be seismically deficient. Total project costs are expected to be \$1.7 million.

**3. Capital Outlay BCP: Vacaville Correctional Medical Facility, Wings U, T, and V.** The Department of General Services requests \$688,000 (Earthquake Safety Bond Funds) for working drawings for the Vacaville Correctional Medical Facility, Wings U, T, and V. DGS has determined these structures to be seismically deficient. Total project costs are expected to be \$3.0 million over four years.

**4. Capital Outlay BCP: Vocational Building at the California Correctional Center in Susanville.** The Department of General Services requests \$331,000 (Earthquake Safety Bond Funds) for preliminary plans and working drawings for the Vocational Building at the California Correctional Center in Susanville. DGS has determined this structure to be seismically deficient. Total project costs are expected to be \$6.5 million over three years.

**5. Capital Outlay BCP: Department of Mental Health Metropolitan State Hospital – Wards 206 and 208 in Norwalk, California.** The Department of General Services requests \$363,000 (Earthquake Safety Bond Funds) for working drawings for the Department of Mental Health Metropolitan State Hospital – Wards 206 and 208 in Norwalk, California. DGS has determined these structures to be seismically deficient. Total project costs are expected to be \$4.4 million over three years.

**6. Capital Outlay BCP: CDC Tehachapi Chapels Facility (Building H).** The Department of General Services requests \$200,000 (Earthquake Safety Bond Funds) for preliminary plans and working drawings for the Chapels Facility (Building H) at the California Department of Corrections Tehachapi facility. DGS has determined this structure to be seismically deficient. Total project costs are expected to be \$2.1 million over three years.

**7. Capital Outlay BCP: Structural Retrofit for the Walker Clinic.** The Department of General Services requests \$225,000 (Earthquake Safety Bond Funds) for working drawings for the California Institute for Women—Walker Clinic at Corona. DGS has determined this structure to be seismically deficient. Total project costs are expected to be \$3.0 million over three years.

**Staff Comments:** At a previous hearing, the Chair requested concrete information from the Administration on the future plans for this facility. According to the CDCR, the CIW

Walker Clinic seismic renovation encompasses the seismic retrofit of the Walker Housing Unit, which the CDCR plans to use to house a 20-bed mother/infant reunification program (referred to as Bonding Mothers with Babies) upon completion of the seismic renovation.

**8. Capital Outlay BCP: California Institute for Women Infirmaries at Corona-Infirmiry Building.** The Department of General Services requests \$224,000 (Earthquake Safety Bond Funds) for working drawings for the California Institute for Women Infirmiry at Corona. DGS has determined this structure to be seismically deficient. Total project cost is expected to be \$2.7 million over three years.

**Staff Comments:** Currently, the CIW Infirmiry seismic renovation project includes retrofitting the Out-Patient Housing Unit (OPHU), wound care clinic, seven medical treatment beds, and the OBGYN clinic. At this time, the OPHU is being used as a temporary Psychiatric Services Unit (PSU) until a permanent structure can be built. The PSU includes 10 single cells for female offenders. CDCR staff indicate that Preliminary Plans for a permanent 20-bed PSU was included in the 2007 Governor's Budget, with funds for Working Drawings and Construction proposed for the 2008-09 Budget. CDCR staff estimate that the construction of the 20-bed PSU will be completed some time during the 2010-11 budget year. Upon completion of the permanent PSU, the 10 single cells in OPHU will be used as a Mental Health Outpatient Housing Unit. All other areas included within the scope of the CIW Infirmiry seismic renovation (wound care clinic, seven medical treatment beds, and the OBGYN clinic) will continue as currently constituted.

CDCR staff indicate that none of the programs/missions identified above are impacted by the 45 bed Intermediate Mental Health Facility that is planned for CIW.

**9. Capital Outlay BCP: Sacramento Public Safety Communications Decentralization.** The budget includes \$4.8 million (various funds) to commence a design phase for the relocation of two critical public safety communications from the top floor of the Resources Building in Sacramento. The Administration seeks to relocate this type of facility from the downtown area to a more seismically sound structure, at a cost of \$29.5 million General Fund.

**10. BCP: Energy Contract Service Attorney.** The Administration requests one attorney position to provide in-house legal services for energy-related legal issues. The Department of General Services' believes their growing involvement in energy purchases and programs necessitates increased staff legal support.

**11. BCP: Baseline Funding Adjustment for Natural Gas Services.** The budget includes \$63.1 million (Service Revolving Fund) to permanently increase the department's baseline natural gas budget up to \$234.3 million, the expenditure level of the current year. This increase is driven by the state's expanded use of natural gas energy, growth in the number of state agency natural gas consumers, and the price of natural gas. The Natural Gas Services Program began in 1997-98 with a budget of \$27 million and has been augmented five times since then, reaching the current level of \$234.3 million.

The CY increase (\$63m) came in a provision request. This request makes that additional funding permanent. The cost factors driving the anticipated increase are number of sites, usage, and price.

**12. BCP: Central Heating and Cooling Plant, Sacramento.** The budget includes an augmentation of \$380,000 (Service Revolving Fund) in the budget year and 2008-09 for private consultant services related to water quality monitoring, regulatory compliance and consultation, and special environmental studies for the waste discharge into the Sacramento River. Unless the department submits meets these water quality requirements, they may be subject to penalties and fines approaching \$25,000/day. The department expects that plant renovations to be completed in 2009 will conclude the need for these consulting services.

**13. BCP: California Public Utilities Commission Building: Special Repairs and Maintenance.** Pursuant to a Memorandum of Understanding between the California Public Utilities Commission and the Department of General Services, the budget includes \$3.1 million (Service Revolving Fund) for special repairs and deferred maintenance at the Edmund G. Brown building in San Francisco.

**14. BCP: Building Maintenance and Operations for Department of Justice Lab Facility, Santa Rosa.** The budget includes \$180,000 (Service Revolving Fund) ongoing to provide custodial, engineering, and grounds keeping services at the Department of Justice's new lab in Santa Rosa. Construction on this facility is nearly complete and it is expected to be ready for occupancy on July 1, 2007.

**15. BCP: CalTrans Building Operations and Maintenance.** The budget includes \$235,000 (Service Revolving Fund) ongoing and three positions to provide building operations and maintenance services at three properties in Sacramento.

**16. BCP: Earthquake Safety Public Buildings Rehabilitation Bond Fund.** The Administration requests to eliminate two positions and \$651,000 in expenditure authority for the Earthquake Safety Public Buildings Rehabilitation Bond Fund. A position to handle project management duties for eight proposed earthquake safety projects would be funded from the Architectural Revolving Fund.

**17. BCP: Secretary of State Building: Conversion to Individual Rate Building.** The Administration seeks \$14.1 million (Service Revolving Fund) to: (a) repair the Secretary of State (SOS) headquarters; and (b) transition the costs of debt service and set up a building rental rate for the SOS to include a six-cents special repairs reserve account to fund future repairs to the building. The department asserts that the SOS does not have the expertise or funds available to ensure the building is properly maintained and repaired and has asked the DGS to manage repayment of debt service and repairs for the building.

**18. Revised Budget Bill Language for Tenant Improvements on DGS Individual Rate Buildings.** In the previous hearing, the Subcommittee heard testimony on the following Budget Bill Language that was agreed to by all parties:

#### **Revised Provisional Language**

9. *The Director of the Department of Finance is authorized to increase this item for purposes of funding tenant improvement projects to facilitate the backfill of vacant space within stand-alone DGS bond funded office buildings. This provision shall only be used to augment expenditure authority for DGS stand-alone individual rate office buildings where a \$0.03 tenant improvement surcharge has been approved by the Department of Finance and is included in the monthly rental rate. Department of Finance approval is contingent upon justification for the proposed tenant improvement projects to be provided by the Department of General Services including an analysis of cost impacts and how the tenant improvements will improve the state's utilization of the facility. Any augmentation made in accordance with this provision shall not result in an increase in any rate charged to other departments for services without the prior written consent of the Department of Finance. Any augmentation made pursuant to this provision may be authorized not sooner than 30 days after notification in writing of the necessity therefore is provided ~~shall be reported in writing~~ to the chairpersons of the fiscal committees of each house and the Chairperson of the Joint Legislative Budget Committee ~~within 30 days of the date the augmentation is approved.~~*

**19. BCP: Conversion of Expiring Positions to Permanent in Office of Public School Construction.** The Administration requests \$1.1 million (\$331,000 General Fund) ongoing to make permanent 13 expiring positions (June 30, 2007) in the Office of Public School Construction (OPSC), Fiscal and Program Services Office. The OPSC asserts that not extending these positions would slow the processing of construction applications for the School Facilities Program. Twelve of these positions were approved in 2004-05 with the understanding that the DGS would seek additional positions as workload needs were refined.

**20. BCP: School Facilities Program Staffing (AB 127).** The Administration requests \$575,000 (2006 School Facilities Fund) and seven permanent positions to support the implementation of Chapter 35, Statutes of 2006 (AB 127). This legislation enabled the construction of new schools to accommodate enrollment growth and modernize existing schools by providing \$7,329,000,000 in general obligation bonds. The proposed staff would better enable the Office of Public School Construction (OPSC) to support this construction effort and accomplish related tasks described in AB 127.

**21. BCP: State Relocatable Classroom Program.** The Administration requests \$4.5 million ongoing (School Building Aid Fund) to cover operating costs and continue the implementation of the phase-out plan for the State Relocatable Classroom Program (SRPC). The request includes \$44,000 to fund travel expenses for the SRCP inspector.

**22. BCP: Office of Administrative Hearings.** The Administration requests to make permanent 73 limited-term Office of Administrative Hearings (OAH) attorney and support positions. These positions do not expire until June 2008 so there will be no fiscal impact in the budget year. The cost to make these positions permanent will be \$9.2 million (Service Revolving Fund) ongoing starting in 2008-09. These staff provide services for the Special Education Dispute Resolution Program, which mediates between school districts and parents of developmentally disabled children. The department has faced difficulty in fully staffing for this program due to the limited-term nature of the existing positions. Funding for these positions is provided through an interagency agreement with the Department of Education (CDE).

**Staff Comments:** At a previous hearing, the Chair requested the DGS to work with staff and to verify this staffing request was consistent with workload. Based on additional information provided by the DGS, staff concerns have been addressed.

**23. BCP: Asset Enhancement of Current Surplus Properties.** The budget includes a one-time augmentation of \$1.6 million (Property Acquisition Law Money Account) for external consultant services to enhance the valuation of three current surplus properties and remediate soil contamination at a Los Angeles property. The proposed consultant services will cost \$1.1 million and the soil remediation \$500,000. The properties to be prepared by a consultant are the Lanterman Developmental Center in Pomona; the Fairview Developmental Center in Costa Mesa; and Los Angeles Civic Center. The Department reports that the sale of these properties has the potential to increase the market value of these properties by as much as \$30 million.

**24. BCP: Infrastructure Studies for DGS Buildings.** The budget includes \$230,000 (Service Revolving Fund) for the preparation of two infrastructure studies of DGS buildings. These studies are normally conducted every 20-25 years. The two buildings to be studied are the Gregory Bateson Building and the State Personnel Board Building, both in Sacramento.

**25. Budget Bill Language to Reappropriate Funding for City of Richmond Hall of Justice and City Hall.**

*1760-492--Reappropriation, Department of General Services.*

*As of June 30, 2007, the balance of the funds appropriated pursuant to Item 1760-101-0768, Budget Act of 1994 (Ch. 139, Stats. 1994), as reappropriated by Item 1760-492, Budget Act of 2003 (Ch. 157, Stats. 2003), Budget Act of 2004 (Ch. 208, Stats. 2004), and Budget Act of 2005 (Ch. 38, Stats. 2005), is reappropriated and shall be available for expenditure until June 30, 2008:*

*Schedule:*

*(1) 3116-Richmond, Contra Costa--City Hall . . . 1,149,975*

*(2) 3117-Richmond, Contra Costa--Hall of Justice . . . 683,613*

*Provisions:*

*1. After June 30, 2008, these funds will no longer be available for expenditure and shall not be reappropriated.*

**26. BCP: Support for Department of Finance's FISCal Project.** The budget includes 18 positions and \$1.9 million (Reimbursements) to support implementation of the Department of Finance's FISCal project. This project seeks to update budget-related IT infrastructure throughout state agencies and the Legislature. The total FISCal request for the budget year (directed by the Department of Finance) is \$35.7 million General Fund and 238 positions.

**STAFF RECOMMENDATION ON VOTE-ONLY ITEMS:** APPROVE issues 1-25 as budgeted. DENY issue 26.

**VOTE on Vote-Only Issues 1-26:**

## 9620      **Payment of Interest on General Fund Loans**

These budget items provide funding for interest payment on General Fund loans and provide that the Department of Finance may adjust these appropriation amounts to make the necessary interest payment, but must notify the Legislature 30 days prior to making any such adjustment.

**Staff Comments:** General Fund cash-flow is uneven over the course of any given fiscal year. The inflow of cash to the General Fund is typically less than the outflow of disbursements during the first 6-8 months of the fiscal year, but this trend reverses in the final 4-6 months. To bridge the gap and meet its cash needs, the General Fund usually borrows funds both internal and external to the state to cover short-term cash needs in anticipation of revenues. The external portion of this cash-flow borrowing is accomplished through the issuance of Revenue Anticipation Notes (RAN). By way of example, on a cash basis for the period ending February 28, 2007, the state spent \$17.2 billion more than it had in General Fund receipts (which totaled \$58.2 billion while disbursements totaled \$75.4 billion). The state started the year with a cash balance of \$9.2 billion, leaving an \$8 billion cash deficit which is addressed by internal borrowing of \$6.5 billion and the issuance of a \$1.5 billion RAN. Similarly, the Governor's Budget anticipates the need to issue a \$3.5 billion RAN in 2007-08.

The RAN allows the state to borrow at low, short-term tax-exempt rates up to an amount limited by federal arbitrage rules. Typically, the size of the RAN proposed is determined by the DOF, the State Controller's Office, and the State Treasurer's Office, and is based on the amount needed to cover any projected cash shortfall and to provide a reasonable cushion to account for uncertainty. The state is free to invest the proceeds of any spare balances at the Pooled Money rate, which is a generally a higher taxable rate.

According to the DOF, the \$3.5 billion RAN in the Governor's Budget is based on minimizing the amount of the state's external borrowing, and does not meet the federal limit. However, the amount of the proposed RAN is subject to change with new fiscal forecasts as a result of the May Revision.

The Subcommittee may wish the Administration and the LAO to:

1. Discuss strengths and weaknesses of the state's existing cash-flow borrowing strategy (of minimizing the state's external borrowing) as it relates to other potential strategies.
2. Comment generally on the factors that are considered in determining what constitutes a reasonable cash "cushion," and the adequacy of the proposed cushion.

**Staff Recommendation:** HOLD OPEN.